

Issue Paper

Brief Description of Topic: Three Tier Task Force Recommendations

Date: January 10, 2007

Presented by: Rick Garza, Deputy Administrative Director, LCB

DESCRIPTION OF ISSUE

The Three Tier Task Force, comprised of stakeholders and LCB staff, presented 11 recommendations to the Liquor Control Board members on December 13, 2006. The LCB will determine how to respond to recommendations and take appropriate action.

BACKGROUND

In March 2006, Governor Gregoire signed Second Substitute Senate Bill (2SSB) 6823. This bill directed the LCB to convene a broad-based Task Force whose charge was to conduct a comprehensive review of the current regulatory system controlling the sale and distribution of beer and wine in Washington State. The Task Force was asked to recommend what, if any, changes should be made to the current regulatory system. The Task Force was specifically directed to:

- Review the genesis of the current regulatory system and whether the system in its current configuration should continue.
- Identify key issues, concerns, and any desired changes by stakeholders about the current system.
- Identify alternatives or modifications to the current system.
- Research and analyze the impacts and implications of 2SSSB 6823, and other suggested modifications to the system on distributors, producers, retailers, and consumers.
- Make recommendations about any proposed changes to the system by December 15, 2006.

The Task Force consisted of 20 diverse stakeholders and a non-voting Chair. Most Task Force members generally agreed that the current system of regulating the distribution and sale of beer and wine could benefit from some changes.

The current Three-Tier system and "Tied House" laws were introduced after the repeal of Prohibition to avoid an imbalance between producers and retailers. Tied House regulations require the financial separation (or independence) of manufacturers from retailers. Manufacturers could no longer be "tied" to the retailer ("house" or tavern) through ownership or other financial interests or create incentives that could also exert undue influence on retailers and ultimately, on consumers.

PROCESS

In April 2006, the LCB contracted with Sterling Associates, LLP to manage and facilitate the Task Force. Sterling also provided independent research, analysis, and support.

Individual and group interviews were conducted with over 100 individuals to identify current system strengths and weaknesses. Eight Task Force meetings were conducted during May through November 2006. The Task Force agreed on recommended changes to state policy goals, which were then used as criteria to assess current regulations and potential changes. The results of the stakeholder interviews were used to help the Task Force focus on key issues and concerns, and to prioritize the Task Force's consideration of alternatives to the current system.

A total of 27 issues were identified and fell into three main categories:

- Sales and distribution.
- Relationship among the tiers.
- Control and enforcement.

The following items were the focus of discussion for Task Force recommendations:

- Price posting and hold.
- Enforcement resources.
- Policy and regulation impact measures.
- General money's worth provisions (including Tied House – Ownership and Financial Interests).
- Ban on quantity discounts.
- Mandatory minimum price mark-up.
- Mandatory (compelled) use of distributors (focusing on common carrier issues).
- Uniform pricing.
- Rules governing LCB retailing of beer and wine.
- Ban on central warehousing.
- Delivered pricing requirements.
- Ban on credit to retailers.

Sterling developed issues papers on key topics to generate discussion among the Task Force. In addition, Sterling conducted independent research, including a 50-state survey. One of the challenges immediately noted is the diversity between states---no two states conduct the business the same way. This makes it difficult to take lessons learned from other states and to review related data for comparison.

The Task Force made 11 recommendations. Three other topics were reviewed and discussed but no majority vote was reached. Without the majority vote, no recommendations were made. The three topics were:

- Ban on central warehousing.
- Distributor's delivery pricing.
- Uniform pricing requirements.

A complete record of the meeting presentations, minutes, research, and appendices are located on the LCB website http://www.liq.wa.gov/3ttf-site/3ttf_intro.html.

RECOMMENDATIONS

The LCB staff offers the following recommendations to the Board members for determining next steps.

*Task Force
Recommendation*

1. State Alcohol Policy

The Task Force believes that an appropriate alcohol regulatory system for beer and wine sales and distribution should be based upon the three policy goals set forth below. In creating and interpreting such a regulatory system, the Legislature and the LCB should consider the economic development of wineries and breweries and related industries, so long as the LCB and the Legislature also consider any adverse impact of any proposals on public health, safety, or welfare. The suggested policy goals are:

- To prevent the misuse of alcohol.
- To promote the efficient collection of taxes.
- To promote the public interest in fostering the orderly and responsible distribution of malt beverages and wine towards effective control of consumption.

*LCB Recommended
Next Steps*

The LCB supports this recommendation.

*Task Force
Recommendation*

2. Tied House Prohibition against Providing Money or Money's Worth to Retailers

The Task Force recommends continuing the state's current approach of adopting specific exceptions to the prohibition against providing money's worth to retailers, and directs the LCB to work with stakeholders to re-examine exceptions and develop a comprehensive list of proposed exceptions for legislative consideration. When developing the list of recommended exceptions, the LCB should consider:

- Industry business needs.
- Customer benefits.
- Whether it creates an unwanted inducement for retailers.
- The potential for increased misuse of alcohol.
- Enforcement resources.

*LCB Recommended
Next Steps*

Convene a work group (internal and external) to evaluate the Tied House Statute. Key objectives will be to identify options and impacts for changing Tied House and to identify consistent criteria that can be used for "exceptions." Recommendations due August 1, 2007.

<i>Task Force Recommendation</i>	<p>3. Tied House Ownership and Financial Interests</p> <p>The Task Force encourages the liberalization of the Tied House ownership restrictions, and recommends that the Legislature work with the LCB to arrive at a workable solution.</p>
<i>LCB Recommended Next Steps</i>	<p>Assign the work group (internal and external) from Recommendation 2 to also evaluate the Tied House Ownership and Financial Interests. Recommendations due August 1, 2007.</p>
<i>Task Force Recommendation</i>	<p>4. Price Posting</p> <p>The Task Force recommends that price posting be eliminated. Note: <i>Price Hold was not recommended for change at this time.</i></p>
<i>LCB Recommended Next Steps</i>	<p>Defer taking any action until the Federal Appellate Court rules on Costco lawsuit in late 2007.</p>
<i>Task Force Recommendation</i>	<p>5. Mandatory Minimum Mark-Up</p> <p>The Task Force recommends elimination of the mandatory minimum mark-up requirement.</p>
<i>LCB Recommended Next Steps</i>	<p>Defer taking any action until the Federal Appellate Court rules on Costco lawsuit in late 2007.</p>
<i>Task Force Recommendation</i>	<p>6. Volume Discounts</p> <p>The Task Force recommends that volume discounts be allowed, with the same volume pricing available to all customers. For example, if a distributor offers price breaks at 10, 100, and 500 units, those price breaks are offered to all customers.</p>
<i>LCB Recommended Next Steps</i>	<p>Defer taking any action until the Federal Appellate Court rules on Costco lawsuit in late 2007.</p>
<i>Task Force Recommendation</i>	<p>7. Use of Common Carriers</p> <p>The Task Force recommends that manufacturers and distributors be allowed to ship their product to retailers using common carriers and consider establishing a licensing requirement for all common carriers delivering alcoholic beverages regardless of origination.</p>
<i>LCB Recommended Next Steps</i>	<p>Convene an internal work group to investigate impacts of allowing manufacturers and distributors to use common carriers. Preliminary recommendations due April 2007.</p>

*Task Force
Recommendation*

8. Credit

The Task Force recommends the state allow the option for manufacturers and distributors to offer credit to retailers with specific terms including a 30-day limit, reporting requirements and penalties for default (temporary license suspension and/or cash penalty).

*LCB Recommended
Next Steps*

Defer taking any action until the Federal Appellate Court rules on Costco lawsuit in late 2007.

*Task Force
Recommendation*

9. Enforcement Resources

The Task Force recommends that the LCB be supported by adequate enforcement resources and that those resources grow in consideration of population increases and increases in liquor licenses.

*LCB Recommended
Next Steps*

Review current staffing level and determine if additional staff is needed. Staffing review is expected to be complete by August 2007. A budget proposal should be developed for the 2008 Legislative session to request additional enforcement resources as appropriate.

*Task Force
Recommendation*

10. General Impact Measures

The Legislature is encouraged to provide funding to the LCB to develop research and analysis capability, and work collaboratively with stakeholders and other agencies and organizations to collect independent data, and to use/analyze existing data.

*LCB Recommended
Next Steps*

An internal workgroup should be convened to identify general impact measures to allow the LCB to collect data to effectively show how policy/rule changes affect the industry, consumers, the state, and society. Recommendations due early 2007.

*Task Force
Recommendation*

11. Measuring Impacts of 2SSB 6823

The Task Force recommends the LCB identify and select key impact measures that can be monitored and analyzed by the Fall of 2007, to provide the Legislature with data about the impacts related to the implementation of 2SSB 6823.

The LCB is encouraged to work with stakeholders and legislative staff to identify the most pertinent impact measures. Key impact measures should be tied to the state's policy goals and should address the impact to industry, consumers, the state and society. And, to the extent possible, consideration should be given to selecting measures for which baseline data are already available. Basic data should be

collected and reported; suggestions include:

- The number of endorsements granted to out-of-state manufacturers and in-state retailers to use the expanded authority.
- The volume of product sold through out-of-state self-distribution.
- The size and type of retailers using the authority.
- Tax revenue collections.

*LCB Recommended
Next Steps*

An internal workgroup should be convened to determine data currently being collected and analyzed. Based on those findings, identify any additional impact measures needed to allow the LCB to collect data to effectively show how policy/rule changes affect the industry, consumers, the state, and society. Recommendations are due by January 31, 2007.

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